

GAO

Report to the Committee on Foreign
Affairs, House of Representatives

May 2009

DEFENSE EXPORTS

Foreign Military Sales Program Needs Better Controls for Exported Items and Information for Oversight



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Why GAO Did This Study

In fiscal year 2008, the Foreign Military Sales (FMS) program sold over \$36 billion dollars in defense articles and services to foreign governments. The Departments of State, Defense (DOD), and Homeland Security (DHS) all have a role in the FMS program. In 2003, GAO identified significant weaknesses in FMS control mechanisms for safeguarding defense articles transferred to foreign governments. In 2007, GAO designated the protection of technologies critical to U.S. national security a high-risk area.

GAO was asked to (1) evaluate program changes State, DOD, and DHS have made since 2003 to ensure that unclassified defense articles transferred to foreign governments are authorized for shipment and monitored as required, and (2) determine what information DOD has to administer and oversee the FMS program. GAO conducted 16 case studies; analyzed U.S. port data and FMS agreements; reviewed program performance metrics; and interviewed cognizant officials.

What GAO Recommends

GAO is making recommendations to State, DOD, and DHS to improve the procedures, processes and information critical for shipment verification, monitoring, and administering the FMS program. State and DHS concurred; DOD concurred with two recommendations and partially concurred with three. GAO believes all recommendations remain valid.

View [GAO-09-454](#) or [key components](#).
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DEFENSE EXPORTS

Foreign Military Sales Program Needs Better Controls for Exported Items and Information for Oversight

What GAO Found

Agencies involved in the FMS program have made some changes in the program but have not corrected the weaknesses GAO previously identified in the FMS program's shipment verification process, and the expanded monitoring program lacks written guidance to select countries to visit to ensure compliance with requirements. State—which is responsible for the program and approving FMS sales—has not finalized proposed regulatory revisions to establish DOD's role in the FMS shipment verification process, although the FMS agencies reached agreement on the proposed revisions about a year ago. DHS port officials, responsible for export enforcement, also continue to lack information needed to verify that FMS shipments are properly authorized. GAO found six FMS agreements that had unauthorized shipments, including missile components. In one case, 21 shipments were made after the agreement was closed. At the same time, DOD, which administers the FMS program and FMS agreements, lacks mechanisms to fully ensure that foreign governments receive their correct FMS shipments—in part because DOD does not track most FMS shipments once they leave its supply centers and continues to rely on FMS customers to notify the department when a shipment has not been received. With regard to monitoring defense articles once in country, DOD does not have written guidance to prioritize selecting countries for compliance visits using a risk management approach and has not yet visited several countries with a high number of uninventoried defense articles.

DOD lacks information needed to effectively administer and oversee the FMS program. For example, within the last 10 years DOD has twice adjusted the surcharge rate—the rate charged to FMS customers to cover program administration costs—but it does not have information on program costs to determine the balance necessary to support the program in the future. Also, while DOD has a goal to release 80 percent of FMS agreements to a foreign government within 120 days of receiving its request to purchase defense articles, DOD officials stated they do not have the information needed to determine if the goal is reasonable. In addition, DOD lacks information to oversee the program, in large part due to the fact that FMS data reside in 13 different accounting, financial, and case implementation systems. DOD is in the process of defining its requirements for FMS program information before it moves forward with improving its data systems. In the meantime, DOD is relying on systems that do not provide it with sufficient, comparable data to oversee the program's performance.

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Abbreviations

CBP	Customs and Border Protection
DHS	Department of Homeland Security
DLA	Defense Logistics Agency
DOD	Department of Defense
DSCA	Defense Security Cooperation Agency
DSP-94	State Department form authorizing export of defense articles and services under the FMS program
FMS	Foreign Military Sales
ITAR	International Traffic in Arms Regulations
NATO	North Atlantic Treaty Organization

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United States Government Accountability Office
Washington, DC 20548

May 20, 2009

The Honorable Howard Berman
Chairman
The Honorable Ileana Ros-Lehtinen
Ranking Republican Member
Committee on Foreign Affairs
House of Representatives

Each year, the U.S. government sells billions of dollars of defense articles and services to foreign governments through the Foreign Military Sales (FMS) program. The FMS program is an integral and growing component of U.S. national security and foreign policy; in fiscal year 2008, the program sold over \$36 billion dollars in defense articles and services to foreign governments,¹ which represented a 56 percent increase over fiscal year 2007 sales. The Departments of State (State), Defense (DOD), and Homeland Security (DHS) all have a role in the FMS program. State has overall responsibility for the program and approving FMS sales. DOD administers the program, and DHS ensures that FMS shipments are transferred in accordance with export control laws and regulations.

In 2003, we identified significant weaknesses in the control mechanisms the FMS program uses to safeguard defense articles transferred to foreign governments.² Specifically, we found that in some cases FMS shipments were not properly authorized and that actions were still needed to implement statutory end-use monitoring requirements to ensure that foreign governments adequately protect U.S.-provided defense articles. These findings along with others prompted us to designate a new high-risk area in 2007: ensuring the effective protection of technologies critical to U.S. national security interests.³ Subsequently, in March 2008, DOD disclosed that it had mistakenly transferred intercontinental ballistic

¹Fiscal year 2008 sales include \$29.2 billion in defense articles and services purchased by foreign governments through the FMS program, as well as \$7.2 billion in articles purchased with U.S. government funds and transferred to foreign governments, such as Iraq and Afghanistan, through the FMS program.

²GAO, *Foreign Military Sales: Actions Needed to Provide Better Controls over Exported Defense Articles*, GAO-03-599 (Washington, D.C.: June 5, 2003).

³GAO, *High Risk Series: An Update*, [GAO-07-310](#) (Washington, D.C.: January 2007).

missile parts to Taiwan through the FMS program, raising questions about whether previously identified weaknesses have been resolved.

Based on your interest in how agencies have addressed weaknesses in the FMS program and how well the program is being managed, you asked us to provide an update on the FMS program. Specifically, we (1) evaluated the FMS program changes State, DOD, and DHS have made since 2003 to ensure that unclassified defense articles transferred to foreign governments are authorized for shipment and monitored as required, and (2) determined what information DOD has to administer and oversee the FMS program.

To conduct our work, we reviewed laws, regulations, and guidelines related to the FMS process. We obtained data from two of the top ten U.S. ports in terms of the dollar value of FMS shipments they process to determine if previously identified gaps in shipment process controls still exist⁴ and conducted 16 case studies to assess steps in the FMS process. The cases were selected to provide variation in military service, foreign customer, type of defense article sold, and transportation method to the end destination. We also analyzed FMS sales agreement data from fiscal years 2003 to 2008. In addition, we interviewed representatives from State; the Defense Security Cooperation Agency (DSCA), the Army, Navy, Air Force, and other DOD components; and DHS's Customs and Border Protection (CBP). Appendix I includes additional details about our scope and methodology. We conducted this performance audit from May 2008 through April 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Results in Brief

State, DOD, and DHS have made some changes in the program but have not corrected weaknesses we previously identified in the FMS program's shipment verification process, and DOD's expanded monitoring lacks written guidance for selecting countries for compliance visits. First, State has not finalized its regulations to establish DOD's role in the FMS shipment verification process, and CBP port officials lack information

⁴These data do not allow us to determine the extent of gaps in controls at all ports.

needed to verify that FMS shipments are properly authorized. As a result, of the port data we reviewed, we found six FMS sales agreements where CBP permitted shipments of defense articles to the foreign country even though DOD records showed that shipments were no longer authorized under the agreements. CBP officials stated that a planned centralized data system could provide the needed information to port officials so they can verify FMS shipments, but the planned system does not currently have funding to include such export information. Second, DOD lacks mechanisms to fully ensure the correct FMS shipments reach the right foreign customers—in part because DOD does not track most FMS shipments once they leave DOD supply centers and continues to rely on the foreign governments to notify the department when a shipment has not been received. Finally, since 2003, DSCA personnel have led teams to visit 19 out of 76 countries that have purchased sensitive defense articles, such as Stinger missiles, under the FMS program. However, DOD does not have written guidance to prioritize compliance monitoring visits using a risk management approach, and DSCA has not yet conducted such visits in countries with a high number of uninventoried defense articles.

DOD also lacks the information needed to effectively administer and oversee the FMS program. For example, within the last 10 years DOD has twice adjusted the administrative surcharge rate to cover FMS program administration costs without knowing if the rates reflect the true cost to administer the program. Without this information, DOD may not have sufficient resources to pay for needed current and future administrative activities. While DOD modified its guidance to clarify when DOD can be reimbursed for additional costs associated with an individual sales agreement, it may be difficult to apply this general guidance to specific FMS agreements, potentially resulting in customers being charged for activities that should be covered by the standard administrative surcharges. DOD also lacks the information needed to develop improved metrics to assess the performance of a key part of the program. While DOD has a goal to release 80 percent of FMS agreements to a foreign government within 120 days of receiving its request to purchase defense articles, DOD officials determined they do not have the information needed to adjust this goal and are reviewing it to determine if it is reasonable. Finally, DOD's ability to obtain comparable information to oversee the program is limited due in large part to its reliance on 13 different accounting, financial, and case implementation systems. DOD is in the process of identifying solutions to improve the data it collects, but is currently relying on systems that do not provide it with sufficient, comparable data to oversee the program's performance.

In addition to reiterating a recommendation to State from our 2003 report, we are making recommendations to State, DOD, and DHS aimed at improving the procedures, processes, and information critical to verify FMS shipments, monitor FMS defense articles, and administer and oversee the FMS program. State and DHS concurred with our recommendations and outlined actions they will take to implement them. DOD concurred with our recommendations to improve procedures for verifying and tracking FMS shipments. DOD partially concurred with our recommendations on providing information to port officials, monitoring FMS defense articles, and improving the information it has to administer and oversee the FMS program. In its response, DOD agreed to provide information to port officials for new FMS agreements but wanted to assess the resources needed to do so for existing agreements before fully implementing the recommendation. DOD also stated that while it was possible to have written guidance for country monitoring visits, any such guidance must be flexible. DOD has reported that it uses a risk-based approach for its monitoring program and as such should establish written guidance for country compliance visits that is consistent with this approach. In addition, DOD said it has sufficient information for program administration. However, DOD's current information is limited for assessing the cost to administer the program and to develop improved metrics. We therefore believe our recommendations remain valid. DHS and DOD also provided technical comments, which we incorporated into the draft report as appropriate.

Background

The Arms Export Control Act authorizes the sale of defense articles and services to eligible foreign customers under the FMS program. Under the program, the purchased items must be used and secured properly by the customer and cannot be sold to third parties. Also, the FMS program must be administered at no cost to the U.S. government. To recover administration costs, DOD applies a surcharge to each FMS agreement that is a percentage of the value of each sale. Multiple organizations have a role in the FMS program, including DSCA and the military services,⁵ State, and CBP. DOD's responsibilities, which are described in the Security Assistance Management Manual, largely focus on the overall

⁵In addition to the military services, other agencies, such as the National Security Agency and the Defense Logistics Agency, can implement FMS agreements.

administration of the program and FMS agreements.⁶ DSCA carries out key functions, such as managing the FMS administrative surcharge account and supervising end use monitoring of FMS items, and the military services carry out the day-to-day implementation of FMS agreements. State regulates the export of defense articles, including the implementation of the FMS program, through its International Traffic in Arms Regulations (ITAR),⁷ and CBP enforces export control laws and regulations at U.S. ports and monitors the dollar value and quantity of defense articles exported under each FMS agreement.

Typically, the FMS process begins when a foreign government submits a letter of request to State or DOD to purchase defense articles under the FMS program. The request is then forwarded to the military service responsible for the particular defense article, which then develops a letter of offer and acceptance, or a sales agreement between the United States and the foreign government. State and DOD officials approve the sale, and Congress is notified if the proposed sale meets certain dollar thresholds and other requirements.⁸ The military service sends the agreement to the foreign government for its acceptance. After the foreign government accepts the agreement, case managers within the military services can begin carrying out agreement actions such as contracting to procure defense articles, issuing requisition orders, providing program management, transporting defense articles if required, and administering financial transactions.

A single FMS sales agreement may result in hundreds or thousands of individual shipments to a foreign government. In most cases, the military service provides the defense article to the foreign country's freight

⁶ In addition to the Security Assistance Management Manual, DOD 5105.38-M, DOD security cooperation responsibilities are included in directives such as DOD Directives 5105.65 and 5132.03.

⁷ 22 C.F.R. §§ 120-130.

⁸ Congress must be notified about FMS sales of major defense equipment that total \$14 million or more, other defense articles or services that total \$50 million or more, or design and construction services that total \$200 million or more. For FMS sales to NATO countries, Japan, Australia, the Republic of Korea, and New Zealand, these dollar values increase to \$25 million, \$100 million, and \$300 million. The proposed sale can only proceed if Congress does not enact a joint resolution prohibiting the agreement within specific time frames. Major defense equipment is equipment that is identified on the U.S. Munitions List as requiring special export controls and for which the U.S. government incurred more than \$50 million in non-recurring research and development costs or more than \$200 million in total production costs.

forwarder, the authorized agent for the foreign customer. However, some countries use DOD's defense transportation system to ship defense articles.⁹ The ITAR requires that freight forwarders register with State, which must receive a letter from the foreign government designating the registered freight forwarder as its authorized agent. CBP port officials rely on a list provided by State to confirm that the freight forwarder for a shipment is the registered freight forwarder for the foreign government. CBP port officials also verify export documentation and subtract the value of each shipment from the total value of exportable goods for each FMS agreement. If the items shipped are incorrect or damaged upon receipt, the foreign government submits a supply discrepancy report to the military service.

Every FMS sales agreement has certain security requirements, including end-use monitoring requirements.¹⁰ To provide reasonable assurance that the foreign customer complies with these requirements, DSCA established the Golden Sentry end-use monitoring program in 2001. As part of this program, security assistance officers stationed in a foreign country monitor the use and security of defense articles purchased through the FMS program, and the officers conduct additional checks on certain sensitive defense articles such as Stinger missiles. DSCA officials conduct regional forums and familiarization visits where the foreign country and DOD representatives work together to mutually develop effective end-use monitoring compliance plans. In addition, DSCA officials conduct country visits to review and assess compliance with the requirements of the FMS agreement and perform investigative visits when possible end-use violations occur.¹¹

⁹ According to the Security Assistance Management Manual, once the title passes to the customer, the customer is generally responsible for the physical movement beyond the initial point of shipment. The Defense Transportation System can be used for all shipments, but generally is used when the customer does not have the resources to perform their own transportation arrangement, hire their own freight forwarders, or when the categories of material are not eligible for transportation through commercial channels.

¹⁰ All defense articles and services purchased through the FMS program must be provided the same degree of security protection as provided by the U.S. government. In addition, each FMS agreement may list individual security requirements for specific defense articles sold under the agreement, such as inventory and physical security requirements.

¹¹ Possible end-use violations include unauthorized third-party transfers, inappropriate use, or tampering.

We have previously reported on weaknesses in the FMS program, including lack of accountability for shipments to some foreign countries, lack of information on end use monitoring, and insufficient information on the costs to administer the program.¹² Table 1 outlines our previous findings.

Table 1: Prior GAO Findings on FMS Program Weaknesses

Program area	Finding
FMS shipments	<ul style="list-style-type: none">Weaknesses in shipment control mechanisms identified; the U.S. government agencies could not ensure that FMS shipments were properly authorized or received by the appropriate foreign government.DOD did not track FMS shipments to verify receipt.
End use monitoring	<ul style="list-style-type: none">DOD lacked sufficient information to determine the resources required to implement end-use monitoring requirements and comply with reporting requirements.
FMS administration	<ul style="list-style-type: none">DOD lacked sufficient information to determine the administrative costs of the program.Changes to the administrative surcharge were made without sufficient analysis to determine the need for or impact of a change.

Source: Previous GAO reports.

Weaknesses in Shipment Verification Process Continue, and Expanded Monitoring Program Lacks Guidance for Country Visits

Agencies responsible for the FMS program have not taken the actions needed to correct previously identified weaknesses in the FMS shipment verification process, and DOD’s expanded end-use monitoring program lacks written guidance for selecting countries for compliance visits using a risk-based approach. First, agencies are not properly verifying FMS shipment documentation, in part because State has not finalized revisions to the ITAR to establish DOD’s role in the verification process. Second, DOD lacks mechanisms to fully ensure foreign governments receive their FMS shipments—in part because DOD does not track most FMS shipments and continues to rely on FMS customers to notify the department when a shipment has not been received. Finally, while DOD has visited an average of four countries each year since 2003 to assess compliance with FMS agreement requirements, it does not have written guidance using a risk-based approach to prioritize the countries it visits to monitor compliance and has not yet visited several countries with a high number of uninventoried defense articles.

¹² See GAO-03-599 and GAO, *Foreign Military Sales: Efforts to Improve Administration Hampered by Insufficient Information*, [GAO/NSIAD-00-37](#) (Washington, D.C.: Nov. 22, 1999).

Agencies Lack Adequate Export Information to Verify FMS Shipments

To control the export of FMS defense articles, freight forwarders are required to provide the following information before CBP allows an FMS shipment to leave a U.S. port: the FMS sales agreement, State’s export authorization form (DSP-94), and evidence that shipment data was entered in the government’s Automated Export System (see table 2).¹³ CBP port officials review this information to confirm that the items are authorized under the FMS agreement and that the agreement has an exportable value remaining. The officials also subtract the shipment’s value from the total value of the defense articles permitted under the FMS agreement.

Table 2: FMS Export Documentation

Document	Description
FMS agreement	<ul style="list-style-type: none">• Describes the items sold under the agreement in general terms.• States the total value of the exportable defense items in the agreement.• Lists administrative and other charges.
Export authorization form for FMS sales, form DSP-94	<ul style="list-style-type: none">• States the dollar amount available for export on a particular FMS agreement.• Identifies the exported defense item’s U.S. Munitions List category.• Bears the authorizing signature of an official of the foreign government or its designated freight forwarder.
Automated Export System information	<ul style="list-style-type: none">• Identifies the FMS agreement by case identification number.• Provides information about the items contained in the shipment.

Source: GAO analysis of State regulations and CBP guidance.

Although we recommended in 2003 that State revise the ITAR to clearly establish control and responsibility for all FMS shipments, it has yet to do so. Shortly after our report, representatives from State, DSCA, and CBP met to draft proposed ITAR revisions that would require DOD to verify that the correct value and type of defense article is listed on the export documentation. According to agency officials involved in the process, agency representatives went through multiple iterations of the draft ITAR revisions over a period of several years. However, these revisions have been in State’s final clearance stages since May 2008. In the meantime, weaknesses we previously identified in the verification process continue to go unaddressed. Anticipating the ITAR updates, in 2004 DOD issued guidance in its Security Assistance Management Manual instructing the military services to verify that the sales value listed on the DSP-94 by the freight forwarders includes only the value of the exportable defense

¹³ The Automated Export System is an interagency export information database managed by the Department of Commerce.

articles listed in the FMS agreement.¹⁴ However, because the guidance only applies to DOD and not the freight forwarders, we found cases where freight forwarders did not submit DSP-94 forms for DOD review. For example, in 10 of our 16 case studies, freight forwarders—who are not bound by DOD’s guidance—did not submit DSP-94s to the military services for verification. In addition, in the six cases that were verified by the military services, one listed the full FMS agreement value on the DSP-94, including administration charges, rather than only the value of the exportable defense articles, as DOD policy requires. Further, officials from one military service were uncertain who within their security assistance command was supposed to verify the documents and how they were supposed to be verified.

CBP port officials lack key information in export documentation that is needed to properly record the value of defense articles shipped under an FMS sales agreement and ensure the value of the shipments made are not more than the exportable value of the agreement. According to CBP guidance, each FMS agreement should have one port that records the value of the exports made against an agreement.¹⁵ However, freight forwarders are not required to identify the primary port on the DSP-94 they provide to CBP at the time of the shipment. For example, freight forwarders listed multiple ports on this form for several of the agreements we reviewed. In one case, the DSP-94 listed seven ports. While information from the Automated Export System is required to accompany all FMS shipments, we found that this system only lists the port of export—not the primary port. CBP port officials have told us that they have no way of knowing if an FMS agreement or a DSP-94 is filed at more than one port because CBP does not have a method to prevent these documents from being filed at multiple ports. Without accurate and complete information on the primary port, officials at other ports cannot notify the primary port regarding shipments that are made through their ports so that the value of these exports can be properly recorded. In some cases, port officials were reducing the exportable value of FMS agreements at ports that were not the primary port. For example, two ports contained duplicate entries for

¹⁴Defense services and administrative charges should be excluded from the value listed on the DSP-94 to ensure that port officials only allow shipments against an FMS agreement equal to the value for exportable defense articles.

¹⁵According to the U.S. Customs Control Handbook for Department of State Licenses, one port should hold the documentation for an FMS sales agreement. This port is supposed to record the value of shipments made against the FMS agreement. In this report, we refer to this port as the primary port for the FMS agreement.

67 FMS agreements, and, for many of these agreements, both ports were independently recording the value of shipments made against the agreement. In one case, the records for one port showed that the agreement value was exhausted, while the records for the second port still showed an exportable value of \$2.9 million.

Although CBP agreed to develop guidelines for FMS shipment verification and reduction of allowable export value after a shipment in response to our 2003 report recommendations, the U.S. Customs Control Handbook for Department of State Licenses has not been updated since 2002, and it does not provide instructions to CBP port officials on tracking shipment and agreement values. CBP issued a policy memorandum in 2004 directing port personnel on how to record shipment values for FMS sales agreements and coordinate with other ports to designate one primary port to track and record shipments against each FMS agreement, but CBP port officials we met with in July 2008 did not have the memorandum, and it was not posted on CBP's intranet, a resource that CBP began to use after 2004 to distribute policy information among the ports.

CBP also lacks adequate information to ensure shipments are not made against closed FMS sales agreements—agreements against which shipments are no longer authorized.¹⁶ In response to a recommendation we made in 2003, DSCA sent quarterly lists of closed cases to CBP in late 2003 and 2004, but rarely did so in subsequent years. Without this information, CBP port officials did not know when an agreement was closed by DOD and only considered the agreement to be closed when the locally recorded exportable value was determined to be exhausted.¹⁷ We compared data from two ports to DOD information on over 2,600 closed FMS agreements¹⁸ and identified 22 FMS agreements that had DSP-94s filed up to 10 years after the closure date of the agreement. CPB port records incorrectly showed that these agreements still had exportable value remaining, which is one of the indicators port officials use to

¹⁶FMS agreements are closed when all ordered articles have been physically delivered, ordered services have been performed, or the FMS purchaser has confirmed that no orders are forthcoming.

¹⁷When an FMS sales agreement is determined to be closed by port officials, they send the FMS agreement documentation, including the authorization form, to the State Department, which archives expired FMS agreements.

¹⁸The list of closed agreements included 467 cases that were identified as closed for the 2003 GAO report and 2212 agreements that were closed from October 2007 to September 2008.

determine if shipments are authorized. We determined that multiple shipments were made against six of these agreements, including agreements for the sale of technical defense publications, avionics components, and missile components. According to DOD officials, one of these agreements was closed before any orders were placed against it; however, we found that 21 shipments were made against this agreement by a freight forwarder. In October 2008, DSCA officials provided a list of recently closed FMS agreements to CBP, and they plan to meet with CBP officials to discuss how to use the information. However, this list only covers agreements that were closed in fiscal year 2008, which could allow shipments to continue to be made against agreements that were closed prior to that time.

In 2003, we recommended that CBP improve its shipment verification process to ensure that it has adequate information to determine when FMS shipments are authorized. However, CBP continues to rely on individual port records and has no method of sharing FMS shipment information among ports. According to CBP officials, only 3 of the more than 100 ports that process FMS shipments maintain an electronic database for recording FMS shipments, but these are not linked to any other system and do not exchange information. Ports without a local database maintain paper copies of FMS documentation and record handwritten notes on the back of DSP-94s to subtract the shipment value from the total case value. CBP officials noted that the Automated Export System allows them to verify that the freight forwarder, defense article, and shipment value match the export documentation, but this system does not allow officials to see the potentially hundreds or thousands of shipments made against an FMS agreement or track the existing exportable value of an agreement. While CBP is in the process of implementing the International Trade Data System, which could automatically subtract the value of individual FMS shipments from the total exportable value of FMS agreements as shipments are made, the system is not scheduled to be completed before 2011 at the earliest. Moreover, at the time of this report, CBP has only received funding to include import information in the system and has not yet received funding for including export information. Although an export component was initially planned, a review of the program may eliminate plans to develop the export component, a step that would prevent the system from improving the FMS process.

DOD Lacks Mechanisms to Fully Ensure That the Correct FMS Shipments Reach the Right Foreign Customers

According to DOD guidance, DOD considers its responsibility for the shipment of FMS articles complete when the title transfers from DOD to the foreign government, which typically occurs when the item is picked up by the freight forwarder at a DOD supply center or other point of origin. DOD does not usually notify the foreign customer when a defense article has been shipped.¹⁹ If a foreign customer has not received an FMS shipment or it is damaged upon receipt, problems that may not be identified until months after the article was shipped, the customer files a supply discrepancy report.²⁰ Each FMS sales agreement may have thousands of shipments associated with it, and discrepancy reports could be filed against each shipment. For example, in our 16 case studies, 188 supply discrepancy reports were filed. Thirty-one of these reports were filed because an incorrect item was received. In such cases, DOD officials may tell the foreign government to dispose of the item and give the foreign government a credit against their account. However, if the report is not submitted within one year, DOD is not required to take action on the discrepancy. If a country chooses not to submit a report, DOD has no procedures in place to identify a lost or diverted FMS shipment as it does not generally track such shipments once they leave the DOD supply center. According to DOD officials, DOD investigates the whereabouts of defense articles that foreign governments claim they did not receive, or received but never ordered, when the foreign customer notifies DOD. Without notification from the customer, DOD may not know when defense articles are mistakenly transferred to a foreign customer. This occurred in 2006 when DOD mistakenly transferred forward section assemblies for the Minuteman III intercontinental ballistic missile to Taiwan instead of the helicopter batteries the country had requested through the FMS program. DOD only became aware of an error in 2007, when Taiwanese officials notified U.S. officials that they did not receive the requested batteries. At the time, DOD did not fully investigate the discrepancy and also did not realize that it had sent missile components to Taiwan until 2008—more than one year after being notified of the error.

¹⁹In certain circumstances, such as when a shipment is oversized or contains hazardous material, DOD will notify the customer or the freight forwarder by sending a notice of availability.

²⁰The customer is responsible for reporting shipping problems by filing a supply discrepancy report within one year of the shipment date. A discrepancy report may be filed for quality deficiency, contractual noncompliance, design deficiency, damaged shipment, shortage-quantity received less than quantity on receipt document, incomplete, unacceptable substitute received, and nonreceipt.

In 2008, the Defense Logistics Agency (DLA) —which manages the inventory for weapon system spare parts and other consumable items in the DOD supply system—took action to ensure that defense articles for shipment are properly labeled in an effort to minimize the risk that an incorrect article is provided to a foreign customer. According to a DLA headquarters official, DLA found it had a high inaccuracy rate for its supply center shipments. DLA inspectors found, for example, that if a shipping label got caught in the printer, the rest of the shipments on the line may have incorrect shipping labels because the personnel on the line may unknowingly skip the jammed label and affix subsequent labels on the wrong packages. DLA's two largest FMS supply depots have recently put in place a double inspection process in which inspectors at the depots ensure that the shipping documentation matches the items in the package. A DLA official stated that this new process should address the problem of improperly labeled defense articles leaving the supply depot—the first part of the shipment process. However, Navy officials responsible for FMS shipments noted that DLA needs to determine the source of the problems to ensure that its solutions are correct. It is too early to know whether DLA's new process will reduce the inaccuracy rate for supply center shipments.

According to DSCA officials, while DOD currently does not track all shipments under FMS sales agreements, it has mechanisms intended to improve visibility over shipments in limited circumstances. For example, DOD established the Enhanced Freight Tracking System, which is intended to allow DOD personnel, freight forwarders, and foreign customers to track shipments from their point of origin to their final destination. Currently, participation by FMS customers is voluntary. DSCA and military service officials stated that the system was designed for customers to track their shipments, and the officials do not plan to use the system to track all FMS shipments. DOD also faces challenges in successfully implementing the new system. First, the system is in the first phase of implementation, which focuses on tracking defense articles from the initial location in the military depot to the freight forwarder, and subsequent phases will allow for shipment tracking to the final destination in the foreign country. Second, in some cases the transportation control numbers that are used to track shipments have been incomplete or changed when shipments were consolidated and therefore are not a reliable method to track shipments. According to DOD officials, while the freight tracking system has multiple searchable fields, for some FMS shipments the transportation control number is the only searchable field. In addition, DOD officials identified another mechanism for tracking FMS shipments that is being used for countries within the U.S. Central

Command area of responsibility, in particular Iraq and Afghanistan. All such shipments are required to have radio frequency identification tags that allow for electronic tracking of shipments through the Enhanced Freight Tracking System to their destination. DSCA officials noted that DOD developed this requirement to address the unique security situation in those countries, and DOD does not have plans to expand it to include shipments to other countries.

DSCA Does Not Have Guidance for Prioritizing Selection of Countries for Compliance Monitoring Visits

In 2003, we found that DSCA lacked the information needed to implement and report on its Golden Sentry end-use monitoring program. Since then, DSCA expanded this program and has been reporting annually on its resources. According to DSCA's fiscal year 2009 monitoring report to Congress, the purpose of the program is to scrutinize the foreign purchaser's use of U.S. defense articles to ensure compliance with U.S. security requirements. The report further notes that to conduct end-use monitoring with available resources, DSCA uses a risk-based approach. Countries are to secure all defense articles purchased through the FMS program. They are also required to maintain a detailed inventory of every item received by serial number for 16 defense articles DOD designated as sensitive. These sensitive defense articles have been purchased by 76 countries and include night vision devices, communication security equipment, and certain types of missiles, such as Stingers.

To ensure that foreign governments and security assistance officers are complying with monitoring requirements, DSCA headquarters officials lead in-country compliance visits, which DSCA has identified as an important part of the Golden Sentry program. Specifically, the visit objectives are to:

- assess in-country security assistance officers' overall compliance with the end-use monitoring program;
- assess the foreign government's compliance with specific physical security and accountability agreements through facility visits, records reviews, and reviews of local security policies and procedures;
- conduct routine or special inventories of U.S.-origin defense articles; and
- appraise possible violations of the U.S. laws, international agreements, or FMS agreements.

To conduct these compliance visits, DSCA assigned three officials to particular regions of the world. These DSCA personnel periodically lead teams made up of several military service and overseas DOD personnel with expertise on sensitive weapon systems or the country visited. DSCA

budgeted \$1.4 million for such visits in each of the fiscal years 2006 through 2008.

Since DSCA began conducting compliance visits in 2003, it has visited 19 countries—or 25 percent—of the 76 countries that have purchased sensitive defense articles, averaging about four visits per year. According to DSCA policy, DSCA compliance visits should focus on the countries that have purchased sensitive defense articles, with a particular emphasis on visiting those with Stinger missiles. DSCA officials stated that they determine compliance visits based in part on foreign policy considerations, such as the need to coordinate visits with foreign governments to respect their sovereignty. While no written guidance exists, officials stated they consider a variety of risk-based factors in determining countries to visit, including considering whether the country is in a stable region of the world or if the officials have information indicating sensitive defense articles may not be properly protected or inventoried. Yet, out of the 19 countries they visited, about 50 percent were in a stable region of the world. In addition, DSCA has not yet conducted compliance visits in three countries that have a high number of uninventoried defense articles, including Stinger missiles and related components and night vision devices, as identified by DSCA's data system. According to a DSCA official responsible for the compliance visits, these three countries are now scheduled for visits in 2009. DSCA also noted that one of these countries needed assistance to help it meet standards before it could have a successful compliance visit. However, as DSCA has not created written guidance for selecting countries for compliance visits, it is unclear how it applied a risk-based approach in prioritizing its country selections to date.

DOD Lacks Information Needed to Effectively Administer and Oversee the FMS Program

While DOD has implemented initiatives aimed at improving the overall administration of the FMS program, it lacks the information needed to effectively administer and oversee the program. First, DOD does not have information on the actual cost of administering FMS sales agreements and, as a result, is not able to link the administrative surcharge DOD charges foreign customers with actual costs. Second, DOD lacks information for determining an improved metric to measure the timeliness with which FMS agreements are developed. Finally, DOD does not have consistent data from each of the military services on administering FMS agreements.

DSCA Lacks Sufficient Information to Determine Administrative Surcharge Rate

Over the past decade, DSCA has implemented several initiatives aimed at improving the balance between FMS expenditures and income. Specifically, DSCA has twice adjusted the surcharge rate—the rate charged to FMS customers to cover program administration costs. However, DSCA does not have sufficient information to determine the balance necessary to support the program in the future. In 1999, DSCA decreased the surcharge rate from 3 to 2.5 percent because the administrative surcharge account had a surplus. Prior to this change, we recommended that DSCA not lower the rate until it determined the cost of implementing the FMS program. However, DSCA disagreed with this recommendation and lowered the rate despite declining income that the program experienced between 1995 and 2000. According to DSCA officials, by 2005 the program experienced a decrease in income that raised concerns about DSCA's ability to pay FMS program expenses if sales continued at the existing rate. Following a year-long internal study to determine a sustainable rate, DSCA increased the surcharge rate from 2.5 to 3.8 percent in August 2006 and clarified what services are included in the administrative surcharge and what services require additional charges.²¹ Since then, the administrative surcharge account balance has grown—a result of both the increased rate and higher than anticipated sales. In fiscal year 2008 alone, FMS program sales totaled \$36 billion—almost triple the amount DSCA had previously projected.

Once the customer signs the agreement and pays the required deposit, DSCA collects 100 percent of the administrative surcharge from agreements in support of the Global War on Terrorism and other agreements with different funding sources²² and 50 percent of the administrative surcharge for all other agreements.²³ Expenditures from these sales agreements continue throughout the entire life of the agreement, which on average last 12 years. However, DSCA knows only historical costs associated with the overall program, not the costs to implement each FMS agreement. Identifying the costs of administering the FMS program is a good business practice identified in federal financial

²¹Other initiatives stemming from the study include instituting a minimum surcharge for low dollar value agreements and the elimination of the logistics support charge as a separate charge.

²²These agreements are known as “pseudo” FMS.

²³The remaining 50 percent of the administrative surcharge for non-Global War on Terrorism cases is received through a payment schedule outlined in the sales agreement.

accounting standards.²⁴ DSCA plans to reassess the optimal rate based on the level of sales and estimated expenses, but without data on actual agreement costs, the surcharge rates DSCA establishes may not be sufficient to pay for needed administrative activities. According to a senior DSCA official, while the fund is not currently in danger of becoming insolvent, it is unclear how the current economic situation may affect future sales levels and, therefore, the administrative account balance.

DSCA's selection of its current surcharge rate has also raised issues with FMS customers and the military services regarding which administrative services require additional charges beyond what is included in the standard administrative surcharge. The standard level of service includes services such as the preparation and processing of requisitions. A country that wants services in addition to the standard level of service, such as additional reviews or contractor oversight, is charged separately for those services. DSCA has provided guidance and training to help the Army, Navy, and Air Force apply the revised standard level of service to new cases. However, according to Navy officials, measuring one standard level of service is unrealistic because every case is unique and may require varying levels of service. Several FMS customer representatives to the Foreign Procurement Group²⁵ also raised questions about administrative surcharge billing and the consistency with which the standard level of service was applied across the services. A briefing prepared by the Foreign Procurement Group in July 2008 noted improvement in the application of the standard level of service but identified the need for additional transparency in DOD's charges for the standard level of service for FMS agreements. For example, the group cited incidences of charging customers for services that should be covered under the standard level of service.

²⁴ Federal financial accounting standards state that reliable information on the costs of federal programs and activities is crucial for effective management of government operations. See *Managerial Cost Accounting Concepts and Standards for the Federal Government*, Statement 4 (July 31, 1995).

²⁵ The Foreign Procurement Group is made up of Washington, D.C.-based foreign government representatives who meet periodically to discuss their experiences with U.S. security assistance programs, including FMS.

DSCA Lacks Sufficient Information to Improve Metric Regarding FMS Agreement Development Time Frame

In an effort to ensure FMS sales agreements are developed and presented to customers in a timely manner, DSCA established a goal of developing and presenting 80 percent of agreements to its customers within 120 days of receiving a request to purchase a defense article through the FMS program. DSCA's 120-day time period begins with the initial receipt of the purchase request and includes the time required to receive pricing information for defense articles from contractors, to allow the services to write the actual FMS agreement, and for all of the relevant agencies to review and approve the sale of the defense articles. In 2008, DSCA began a study to determine if the 120-day goal was reasonable or if it needed to be revised. However, DSCA officials stated they did not have sufficient information to make such a determination. As a result, DSCA directed each military service to study its FMS process to assess internal FMS processes and the time frames associated with those processes. According to DSCA officials, they anticipate receiving the results of the studies in early summer 2009.

A variety of factors may affect the military services' ability to meet the 120-day time frame for developing an FMS agreement. For all agreements implemented from January 2003 to September 2008, DSCA developed 72 percent of FMS agreements within its stated 120-day goal. While it takes an average of 122 days after the initial receipt of a request to develop an FMS agreement, the number of days that it took to develop an FMS agreement ranged from less than one to 1,622 days.²⁶ While DSCA officials noted that the creation of a central agreement writing division in 2007 has helped improve the consistency of agreements, there are other factors affecting the time it takes to develop an agreement. Officials responsible for developing the FMS agreements stated that while it is possible to meet the 120-day goal on routine agreements, such as blanket order agreements,²⁷ it is difficult to meet the goal for complex agreements, such as agreements for weapons systems. Agreements over certain dollar thresholds could require more time if they have to go through the congressional notification process. Similarly, for example, non-NATO cases may require more time for the U.S. Embassy in the customer country to conduct an evaluation of

²⁶In some cases, the FMS agreement is written the same day that the request to purchase defense articles is received.

²⁷A blanket order agreement is an agreement between a foreign customer and the U.S. government for a specific category of items or services (including training) with no definitive listing of items or quantities. The case specifies a dollar ceiling against which orders may be placed.

the proposed sale. Prioritization of certain agreements, such as Iraq FMS agreements, can also delay the development of other FMS agreements. Other factors that can extend FMS agreement development times include slow customer response to follow-up questions about requests to purchase defense articles, workload challenges within the military services, and slow contractor response times for pricing information about the defense article the foreign government wants to purchase.

**Disparate Data Systems
Limit Available
Information for DSCA
Oversight of FMS Program**

FMS implementation, management, and financial data—which DOD uses to track, oversee, and execute FMS sales agreements—are currently dispersed among 13 electronic systems across the military services and other DOD components. As a result, DSCA’s ability to obtain FMS program information and to manage the efficiency of the FMS process is limited. For example, one DSCA official responsible for collecting program information noted that DSCA cannot effectively measure cost, schedule, and performance on FMS agreements because current systems only provide three consistent indicators that are comparable across the military services. According to the official, while the service specific systems may provide information for analyzing the performance of FMS agreements within that service, the information is not comparable with data produced by other services, thus reducing its value to DSCA for overall oversight of the program. DSCA compiles the limited available data from the military services for quarterly meetings that review the FMS program in an effort to determine potential problems. In addition, as DOD does not have a centralized system, the services have independently developed tools to enhance the capabilities of their existing systems, one of which has been in place since 1976.²⁸ For example, the Air Force independently developed a web-based system for processing supply discrepancy reports, but DSCA has yet to fully fund this system to be used by the other services.

In an effort to develop more comparable, detailed, and complete data on agreement implementation, DSCA is working to develop the Security Cooperation Enterprise Solution. DSCA is currently defining the requirements for this potential system and has yet to determine how it will relate to other data systems. According to DSCA officials, recent increases in FMS sales and the administrative surcharge rate will provide sufficient funds to begin the development of a new data system. DSCA also uses the

²⁸DSCA issued a memorandum in 1998 requesting that major enhancements to the service specific systems be coordinated through DSCA until it developed a centralized data system.

Security Cooperation Information Portal—a web-based tool designed to provide a point of access for DOD’s multiple FMS information systems, such as the services’ requisition systems, the system used to write agreements, and the financial systems. The portal retrieves information from existing DOD systems and is intended to provide consolidated information to DOD and foreign customers. However, as the portal is based on information from 13 different systems, the data have the same limitations in providing DSCA with comparable data to oversee the FMS program.

Conclusions

The FMS program, as a part of a broader safety net of export controls designed to protect technologies critical to national security as well as an important foreign policy tool to advance U.S. interests, presents a set of unique challenges to the agencies involved in the program. Previously identified weaknesses in the FMS shipment verification process remain unaddressed and require the immediate and collective attention of leadership within State, DOD, and Homeland Security. While these departments each have a distinct role to play in the FMS program, they have failed to work collectively to ensure that FMS articles are not vulnerable to loss, diversion, or misuse. This failure has clear national security implications because defense articles will be at risk of falling into the wrong hands. Consistent with our 2003 report, we still believe that State should revise the ITAR to establish procedures for DOD verification of FMS shipments to address weaknesses in the shipment verification process. Also, DOD may not be maximizing its resources by fully applying a risk-based approach to ensure that sensitive defense articles are protected as required. In addition, DOD has made changes to its FMS program administration without sufficient information on which to base these changes, and it lacks information to assess how well the program is working. Without this information, DOD’s ability to know if the program is achieving intended results is limited.

Recommendations for Executive Action

To improve controls for exported items as well as administration and oversight of the FMS program, we are reiterating a recommendation to State from our 2003 report and making the following five recommendations.

To establish procedures for DOD verification of FMS shipments, we recommend that the Secretary of Defense direct the Under Secretary of Defense for Policy to provide additional guidance to the military services on how to verify FMS shipment documentation.

To ensure CBP port officials have the information needed to verify FMS shipments are authorized, we recommend that the Secretary of State direct the Assistant Secretary for Political-Military Affairs, that the Secretary of Defense direct the Under Secretary of Defense for Policy, and that the Secretary of Homeland Security direct the Commissioner of Homeland Security's U.S. Customs and Border Protection to coordinate on establishing a process for:

- ensuring the value of individual shipments does not exceed the total value of the FMS agreement;
- designating a primary port for each new and existing FMS agreement;
- developing a centralized listing of these primary ports for use by CBP port officials; and
- providing CBP officials with information on FMS agreements that were closed prior to fiscal year 2008.

To ensure that correct FMS shipments reach the right foreign customers, we recommend that the Secretary of Defense direct the Under Secretary of Defense for Policy to examine its existing mechanisms and determine if they can be used to improve tracking of FMS shipments.

To ensure that FMS defense articles are monitored as required, we recommend that the Secretary of Defense direct the Under Secretary of Defense for Policy to create written guidance for selecting in-country visits that consider a risk-based approach.

To improve the administration and oversight of the FMS program, we recommend that the Secretary of Defense direct the Under Secretary of Defense for Policy to better determine the administrative costs of implementing the FMS program and develop metrics that allow DSCA to comprehensively assess the performance of the FMS program.

Agency Comments and Our Evaluation

State, DHS, and DOD provided written comments on a draft of this report, which are reprinted in appendices II through IV. DHS and DOD also provided technical comments, which we incorporated as appropriate. In written comments, State and DHS concurred with our recommendations and outlined plans to implement them. DOD concurred with two of our recommendations and partially concurred with the other three. In its technical comments, DOD also noted that it disagreed with our characterization of the information it uses to administer the FMS program.

In concurring with the recommendation that State should revise the ITAR, which we reiterated from our 2003 report, State noted that the Political-Military Bureau is processing the recommended changes to the ITAR and will publish them in the *Federal Register* as soon as all requirements for doing so are met.

DOD concurred with our recommendation to provide additional guidance on verifying FMS shipment documentation and agreed to work with the military services to review the current guidance and revise as necessary. DOD also concurred with our recommendation that it examine its existing mechanisms for tracking FMS shipments and will work with agency representatives to improve end-to-end visibility.

In response to our recommendation that State, DHS and DOD coordinate to ensure CBP port officials have the information needed to verify that FMS shipments are authorized, DHS and DOD agreed to work together to provide this information. DHS identified several specific actions that it plans to take, including reconvening an interagency working group to address FMS-related issues, obtaining a complete list of closed FMS agreements from DOD, and establishing a list of all primary ports for existing and new FMS agreements. DOD also agreed to provide CBP with a list of closed FMS agreements. While DOD agreed to work with State and CBP to establish a process for designating a primary port for each new FMS agreement, it noted that it will have to examine the resource impact of designating a primary port for existing FMS agreements before taking further action. Once DOD has made this assessment it will be important for the agencies to determine the appropriate course of action for existing agreements.

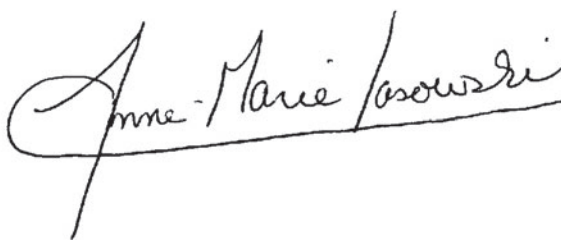
DOD partially concurred with our recommendation to create written guidance for in-country visits and said that such guidelines could be included in the Security Assistance Management Manual. DOD noted that these guidelines would take risk into account, but would have to be broad enough to consider other factors, such as the experience of personnel, when scheduling in-country visits. DOD has reported to Congress that it uses a risk based approach to conduct end-use monitoring with available resources. While our report notes that a variety of factors play a role in the selection of countries for compliance visits, we also found that the current system, which lacks written guidance, may not ensure that DOD is distributing its resources in a risk-based manner. As DOD has identified these visits as an important part of its monitoring program, we continue to believe that DOD needs written guidance—whether in published guidance

or internal policy memos—that applies a risk-based approach to ensure that sensitive defense articles are protected as required.

DOD also partially concurred with our recommendation that it improve the administration and oversight of the FMS program. DOD agreed that rigorous data analysis and well-defined, targeted metrics are vital for FMS program administration. It noted that it conducted a year-long study prior to changing the current administrative surcharge rate in August 2006 and that it hosts a quarterly forum at which security cooperation leadership review metrics related to the FMS program. In its technical comments, DOD also stated that it has sufficient information and that it is not required to gather information on actual costs to administer the FMS program. As we state in our report, DOD's August 2006 study relies on future sales estimates and historical budget data for program administration to develop its surcharge rate, which does not provide it with the actual costs to implement existing FMS agreements. We also note that identifying the costs of administering the FMS program is a good business practice recognized in federal financial accounting standards. In addition, while we acknowledge that DOD officials meet at quarterly forums to review existing metrics, they have limited consistent indicators that are comparable across the military services. As such, we continue to believe that DOD should obtain additional information regarding the cost of implementing FMS agreements and to develop metrics to administer and oversee the program.

As agreed with your office, unless you publicly announce the contents of this report earlier, we plan no further distribution of it until 30 days from the date of this report. We will then send copies to the Secretaries of State, Defense, and Homeland Security. In addition, we will make the report available at no charge on the GAO Web site at <http://www.gao.gov>.

Please contact me at (202) 512-4841 or lasowskia@gao.gov, if you or your staff have any questions about this report. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Key contributors to this report were Ann Calvaresi-Barr, Director; John Neumann, Assistant Director; Heather Miller; Jean Lee; Sarah Jones; Ann Rivlin; Noah Bleicher; John Krump; Karen Sloan; Art James; and Rebecca Rygg.

A handwritten signature in black ink that reads "Anne-Marie Lasowski". The signature is written in a cursive style with a large initial "A" and a long horizontal line extending from the end of the name.

Anne-Marie Lasowski, Director
Acquisition and Sourcing Management

Appendix I: Scope and Methodology

To examine the changes that State, DOD, and DHS have made to the FMS program since 2003, we reviewed the regulatory framework governing the FMS process, including the Arms Export Control Act, the International Traffic in Arms Regulations (ITAR), and a draft of potential revisions to the ITAR. We also reviewed the U.S. Customs Control Handbook for Department of State Licenses, the Defense Department's Security Assistance Management Manual, and other guidance from Customs and Border Protection (CBP), the Defense Department, and the military services. We used case studies to assess the steps in the FMS process. Using data available to the military services and FMS officials through the Defense Security Assistance Management System, we selected 16 FMS agreements based on the following attributes: the military service responsible for administering the FMS agreement, the type of defense item sold, whether the item required enhanced end-use monitoring, the customer country, and agreements that used both the Defense Transportation Service and freight forwarders to transport defense articles to their end destination. We selected similar defense articles to compare across the military services. We obtained data from DOD systems used to manage the FMS program. We verified that the agreements we selected contained the traits for which they were selected. Based upon this verification, we confirmed that the data we used were sufficiently reliable for our purposes. We also obtained data from two major ports, one airport and one seaport. These ports are 2 of the top 10 U.S. ports in terms of the dollar value of FMS shipments they process. We used these data to determine if FMS agreements were being lodged at multiple ports and to determine if exports were occurring against FMS agreements for which exports were no longer authorized. We reviewed copies of licenses and shipment logs to identify when actual shipments were made against FMS agreements that were no longer authorized to have shipments. Our analysis of these data allowed us to determine whether gaps in controls exist, but did not allow us to assess the state of controls at all ports. In addition, we interviewed officials and obtained documentation at the State Department, the Defense Security Cooperation Agency (DSCA), the Air Force Security Assistance Center, the United States Army Security Assistance Command, the Navy International Programs Office, the Naval Inventory Control Point, the Defense Logistics Agency, CBP headquarters and port personnel at two ports, and U.S. security assistance officers stationed in one NATO and one non-NATO country.

To determine the information DOD uses to administer and oversee the FMS program, we reviewed the Defense Department's Security Assistance Management Manual and other guidance from the Defense Department and the military services. We also reviewed the Office of Management and

Budget's Managerial Cost Accounting Concepts and Standards for the Federal Government - Statement of Federal Financial Accounting Standards Number 4. We analyzed data the military services use to manage FMS agreements implemented from fiscal years 2003 to 2008. We conducted interviews with officials at DSCA and the military services. We also met with the Foreign Procurement Group, a group composed of FMS customer countries, to ask them about their experiences with the FMS program and reviewed the group's 2008 briefing for the program. We conducted this performance audit from May 2008 to April 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Comments from the Department of State



United States Department of State

Washington, D.C. 20520

MAY 06 2009

Ms. Jacquelyn Williams-Bridgers
Managing Director
International Affairs and Trade
Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548-0001

Dear Ms. Williams-Bridgers:

We appreciate the opportunity to review your draft report, "DEFENSE EXPORTS: Foreign Military Sales Program Needs Better Controls for Exported Items and Information for Oversight," GAO Job Code 120738.

The enclosed Department of State comments are provided for incorporation with this letter as an appendix to the final report.

If you have any questions concerning this response, please contact Andrew Lim, Foreign Affairs Officer, Bureau of Political-Military Affairs at (202) 647-8155.

Sincerely,

A handwritten signature in black ink, appearing to read "James L. Millette".

James L. Millette

cc: GAO – John Neumann
PM– Kevin O’Keefe
State/OIG – Mark Duda

Department of State Comments on GAO Draft Report

**DEFENSE EXPORTS: Foreign Military Sales Program Needs Better
Controls for Exported Items and Information for Oversight**
(GAO-09-454 GAO Code 120738)

Thank you for allowing the Department of State the opportunity to comment on the draft report "*Defense Exports: Foreign Military Sales Program Needs Better Controls for Exported Items and Information for Oversight.*"

The report recommends making certain revisions to the International Trafficking in Arms Regulations (ITAR). The State Department's Political-Military Bureau continues to process the recommended changes to the ITAR and will publish them in the Federal Register as soon as all requirements for doing so are met.

Appendix III: Comments from the Department of Homeland Security

U.S. Department of Homeland Security
Washington, DC 20528



**Homeland
Security**

May 8, 2009

Ms. Anne Marie Lasowski
Director, Acquisition and Sourcing Management
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Dear Ms. Lasowski:

Thank you for providing us with a copy of the draft report entitled "DEFENSE EXPORT: Foreign Military Sales Program Needs Better Controls for Exported Items and Information for Oversight" (GAO-09-454). In 2003, GAO identified significant weaknesses in foreign military sales (FMS) control mechanisms to safeguarding defense articles transferred to foreign governments. These and other findings prompted GAO to designate the protection of technologies critical to U.S. national security a new high-risk area in 2007. Below is the response to the one recommendation directed to the Department of Homeland Security.

Recommendation 3: To ensure Customs and Border Protection (CBP) port officials have the information needed to verify FMS shipments are authorized, we recommend the Secretary of State direct the Assistant Secretary for Political-Military Affairs, the Secretary of Defense direct the Under Secretary of Defense for Policy, and the Secretary of Homeland Security direct the Commissioner of Customs and Border Protection to coordinate on establishing a process for:

- a. Ensuring the value of individual shipments does not exceed the total value of the FMS agreement;
- b. Designating a primary port for each new and existing DMS agreement;
- c. Developing a centralized listing of these primary ports for use by CBP port officials; and
- d. Providing CBP officials with information on FMS agreements that were closed prior to fiscal year 2008.

Response:

Concur. CBP will re-issue the guidance on decrementation of the FMS cases and obtain a complete list of all FMS closed cases from DSCA.

In addition, CBP will publish guidance specifically on processing FMS shipments and the handling of the cases. CBP will establish a complete list of where all the existing and new FMS cases are lodged and post such list to the CBP Intranet web site.

**Appendix III: Comments from the Department
of Homeland Security**

- 2 -

Moreover, CBP will post information to the CBP Intranet web site about closed cases, port locations for active FMS cases, and procedural guidance on processing FMS cases and shipments.

CBP has requested the re-establishment of the FMS Interagency Working Group to complete the 2003 GAO recommendation. Scheduling for the first meeting is being reviewed by all the participating agencies.

Thank you for the opportunity to provide comments to the draft report.

Sincerely,



Jerald E. Levine
Director
Departmental GAO/OIG Liaison Office

Appendix IV: Comments from the Department of Defense



POLICY

OFFICE OF THE UNDER SECRETARY OF DEFENSE
2000 DEFENSE PENTAGON
WASHINGTON, DC 20301-2000

MAY 15 2008

Ms. Ann Marie Lasowski
Director
Acquisition and Sourcing Management
U.S. Government Accountability Office
441 G Street, N. W.
Washington, D.C. 20548

Dear Ms. Lasowski:

This is the Department of Defense (DoD) response to the GAO Draft Report, GAO-09-454, "DEFENSE EXPORTS: Foreign Military Sales Program Needs Better Controls for Exported Items and Information for Oversight," dated April 10, 2008 (GAO Code 120738).

We have conducted a thorough review of the report. Detailed comments on the recommendations are attached at Tab 1. While we concur or partially concur with all of the recommendations made by the draft report, we have identified several corrections that should be made to improve the overall accuracy of the report. These technical comments are provided at Tab 2. We hope this information is useful to you in finalizing your report.

My point of contact on this matter is Mrs. Beth Baker. She may be contacted by e-mail: beth.baker@dsca.mil or by telephone at (703) 601-3839.

Sincerely,

Peter F. Verga

Attachments
As stated



GAO DRAFT REPORT DATED APRIL 10, 2009
GAO-09-454 (GAO CODES 120738)

**“DEFENSE EXPORTS: FOREIGN MILITARY SALES PROGRAM NEEDS
BETTER CONTROLS FOR EXPORTED ITEMS AND INFORMATION FOR
OVERSIGHT”**

**DEPARTMENT OF DEFENSE COMMENTS
TO THE GAO RECOMMENDATIONS**

RECOMMENDATION 1: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy to provide additional guidance to the military services on how to verify Foreign Military Sales (FMS) shipment documentation. (p. 20/GAO Draft Report)

DOD RESPONSE: Concur. The Defense Security Cooperation Agency (DSCA) will work with the military services to review the current guidance on verifying FMS shipment documents and revise and/or provide additional guidance as required.

RECOMMENDATION 2: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy to coordinate on establishing a process for ensuring the value of individual shipments does not exceed the total value of the FMS agreement. (p. 20/GAO Draft Report)

DOD RESPONSE: Concur. DSCA will work with Customs and Border Protection (CBP) and the Department of State to develop a process to ensure that the value of all individual shipments made do not exceed the total exportable value authorized by the FMS agreement.

RECOMMENDATION 3: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy to coordinate on establishing a process for designating a primary port for each new and existing FMS agreement. (p. 20/GAO Draft Report)

DOD RESPONSE: Partially Concur. DSCA will work with CBP and the Department of State to develop a process for designating a primary port for each new FMS agreement. DSCA would have to examine the resource impact of

making such changes to existing FMS agreements before committing to a change that impacts agreements that have already been implemented.

RECOMMENDATION 4: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy to coordinate on establishing a process for developing a centralized listing of these primary ports for use by CBP port officials. (p. 21/GAO Draft Report)

DOD RESPONSE: Concur. DSCA will work this issue with CBP and the Department of State.

RECOMMENDATION 5: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy to coordinate on establishing a process for providing CBP officials with information on FMS agreements that were closed prior to fiscal year 2008. (p. 21/GAO Draft Report)

DOD RESPONSE: Concur. DSCA is providing a historical list of closed FMS agreements and will continue to provide regular updates to this list.

RECOMMENDATION 6: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy to examine its existing mechanisms and determine if they can be used to improve tracking of FMS shipments. (p. 21/GAO Draft Report)

DOD RESPONSE: Concur. Through the Enhanced Freight Tracking System (EFTS) development process, existing transportation data systems are being used to extract relevant FMS transportation data. By mapping to various external systems, EFTS intends to improve tracking of FMS shipments for all methods of conveyance. Where there is a shortfall in Information Technology and/or a need to track materiel (e.g., Customs, FMS Customer's freight forwarder), DSCA is working with the agency representatives to bridge the requirement for end-to-end visibility of the distribution pipeline.

RECOMMENDATION 7: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy create written guidance for selecting in-country visits that consider a risk-based approach. (p. 21/GAO Draft Report)

DOD RESPONSE: Partially concur. It is correct that there currently is no written guidance for prioritizing Compliance Assessment Visits (CAVs). We agree that written guidelines for selection of countries to receive CAVs could be included in the Security Assistance Management Manual (SAMM) with the understanding that such guidelines will have to be broad enough to take many subjective factors into consideration. The CAV schedule is created with numerous considerations taken into account. Risk is one factor – but even risk is not objective and must consider many subjective elements including (1) The inventory of enhanced items (both in size and make-up), (2) The history of the Golden Sentry program within the host nation, (3) The region of the world in question, and (4) Current or previous reports of concerns relative to the country’s protection of U.S. articles. Any written guidance will be largely as subjective as the current process of determination through internal consultations. Beyond these risk-based factors, elements of maximizing a trip (adding a small program to an existing major program trip), experience of personnel, and other factors can appropriately affect the scheduling of CAVs.

RECOMMENDATION 8: The GAO recommended that the Secretary of Defense direct the Under Secretary of Defense for Policy to better determine the administrative costs of implementing the FMS program and develop metrics that allow DSCA to comprehensively assess the performance of the FMS program. (p. 21/GAO Draft Report)

DOD RESPONSE: Partially concur. We agree that rigorous data analysis is vital to determining proper assessment of administrative costs needed to implement the FMS program. The Arms Export Control Act (AECA), Section 21(3)(1)(A) requires that we recover the full estimated costs of administration of sales using “an average percentage basis.” The current administrative surcharge rate assessed against FMS cases, in compliance with the AECA, is 3.8%. This percentage was effective in August 2006 and was derived only after an intensive year-long study was conducted to review costs, sales projections, workload impacts, etc. DSCA recognizes that fluctuations in customer financial health, regional and world stability conditions, etc. influence FMS programs and impact the surcharge rates needed to ensure these programs can continue to operate at no cost to the U.S. Government. In 2006, DSCA self-imposed a requirement to review the health of the administrative surcharge account annually to determine if the rate is fair and adequate or whether it should be changed to more accurately reflect anticipated costs. DSCA agrees that well-defined, targeted metrics are vital to assessing FMS programs and processes. We host a quarterly forum for leadership in the security cooperation community to review and refine metrics related to FMS and other related programs. Data from these reviews are used to recommend, study, and implement process improvements across our community.

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